Supreme Court, U.S.
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No. 03-772

IN THE
Supreme Court of the United States

AMERICAN GENERAL FINANCE, INC., and
MICHAEL J. ANDERSON,

Petitioners,

v.

MARY JEAN ASHBY,

Respondent.

On Petition for a Writ of Certiorari to the
Supreme Court of Alabama

RESPONDENT'S BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether an arbitration agreement that provides that all disputes relating to arbitrability should be decided by an arbitrator prohibits a court from deciding whether the arbitration agreement is unconscionable under state law.

2. Whether the Alabama Supreme Court properly applied generally applicable state contract law to hold unconscionable an arbitration agreement between a borrower and a lender that compelled only the borrower to use arbitration and limited the borrower's legal remedies, while permitting the lender to seek full relief in either a judicial or arbitral forum.

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INTRODUCTION

The opinion of the Alabama Supreme Court does not warrant this Court's review. That court's holding that an arbitration agreement between petitioner American General Finance (AGF) and respondent Mary Jean Ashby is unconscionable was properly based on generallyapplicable principles of Alabama contract law, and does not conflict with this Court's precedents or the decisions of any lower courts. Moreover, the decision was based on the factual circumstances surrounding the formation of the specific contract in this case, including the trial court's finding that Mrs. Ashby is functionally illiterate and that AGF's agent nonetheless failed to inform her of the existence of the arbitration agreement in the contract she signed. Thus, even if the questions presented concerned issues about which courts had reached conflicting decisions — which they do not — this case would not provide a good vehicle in which to review them.

STATUTORY PROVISIONS INVOLVED

In addition to Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, quoted in the Petition, this case also involves Section 4 of the Federal Arbitration Act, 9 U.S.C. § 4, which provides in relevant part:

> The court shall hear the parties, and upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court

> shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement.

In addition, the case involves Alabama Code 1975, § 5-19-16, which provides:

> With respect to a consumer credit transaction, if the court as a matter of law finds the contract or any provision of the contract to have been unconscionable at the time it was made, the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable provision, or it may so limit the application of any unconscionable provision so as to avoid any unconscionable result.

STATEMENT OF THE CASE

1. Factual Background

a. The Terms of the Loan Between the Ashbys and AGF.

On April 15, 1999, Mary Jean Ashby and her late-husband, Jimmy Ashby, obtained a $2,000 loan from petitioner AGF. Pet. App. 1a. The Ashbys agreed that their pick-up truck would serve as collateral for the loan, and that they would pay off the loan over a three-year

period. *Id.* at 1a, 60a. In addition, Mr. Ashby agreed to purchase $5,000 of credit life insurance during the term of the three-year note from Merit Life Insurance Company, an affiliate of AGF, which required borrowing another $827.10 from AGF. *Id.* at 2a, 60a.

Mr. and Mrs. Ashby obtained the loan agreement and the credit life insurance policy from Michael Anderson, the branch manager for AGF and an insurance agent for Merit. *Id.* at 2a. The Ashbys told Mr. Anderson that they were not able to read the contract because Mr. Ashby was completely illiterate and Mrs. Ashby is functionally illiterate, and they requested that he inform them of the contents of the documents they were signing. *Id.* at 60a. Mr. Anderson told the Ashbys that they were borrowing $2,000 plus $16.50 for a title fee, and $827.10 for credit life insurance, for a total loan of $2,843.60. *Id.* Mr. Anderson further explained that the annual percentage rate on their loan was 23.8% and that they would be required to make monthly payments of $111.27. *Id.* However, as Mrs. Ashby testified and as the trial court found, Mr. Anderson did not tell the Ashbys that the loan and credit life documents contained arbitration provisions. *Id.*

b. AGF's Mandatory Arbitration Clause.

The mandatory and binding arbitration provision in AGF's finance papers with the Ashbys appears to apply to all claims by either party. The arbitration provision begins: "Borrower(s) and lender agree that, except as

otherwise set forth herein in this provision, all claims, disputes, or controversies of every kind and nature between Borrower(s) and Lender shall be resolved by arbitration." Pet. App. 3a. However, several paragraphs later, near the end of the arbitration clause, AGF reserves only for itself the right to sue in court for virtually any claim it could have against the Ashbys:

> Borrower(s) and Lender agree that, notwithstanding the foregoing, Lender retains the right to use judicial or self-help remedies (i) to repossess or foreclose on collateral or to enforce the security interests relating to this transaction, and (ii) to pursue collection actions against the Borrower(s) where the amount of the debt is $10,000 or less.

Id. at 4a. Due to the size of the Ashbys' loans, this saves from the arbitration requirement every foreseeable claim that AGF could ever bring against the Ashbys.

AGF's protection of its own right to sue the Ashbys in court does not extend to any counterclaims raised by the Ashbys in such suits. Instead, AGF retains sole control over the forum for such counterclaims by reserving the right to compel arbitration separate and apart from the litigation of AGF's claims against the Ashbys:

> The exercise of this right by Lender to pursue judicial or self-help remedies shall

> not constitute a waiver of Lender's right to compel the arbitration of any claim or dispute subject to this arbitration clause — including the filing of a counterclaim by Borrower(s) in a lawsuit filed by Lender.

Id. at 4a. The arbitration provision also provides that "all issues and disputes as to the arbitrability of claims must also be resolved by the arbitrator." *Id.* at 3a.

In addition to the unilateral waiver of the Ashbys' right to sue in court, AGF's arbitration provision imposes restrictions on the remedies that are available to the Ashbys in arbitration. Specifically, the arbitration clause limits the amount of punitive and mental anguish damages for which AGF may be held liable to the Ashbys in arbitration, without regard to its culpability:

> BORROWER(S) AND LENDER AGREE THAT THE ARBITRATOR MAY AWARD PUNITIVE DAMAGES ONLY UNDER CIRCUMSTANCES WHERE A COURT OF COMPETENT JURISDICTION COULD AWARD SUCH DAMAGES. HOWEVER, IN NO EVENT SHALL AN AWARD OF DAMAGES EXCEED FIVE (5) TIMES THE ECONOMIC LOSS SUFFERED BY THE PARTY.

Id. at 4a. This arbitration provision also imposes a

unilateral prohibition on the Ashbys' participation in any class action proceedings involving the lender:

> BORROWER(S) AND LENDER FURTHER AGREE THAT THE ARBITRATOR SHALL NOT CONDUCT ANY CLASS-WIDE PROCEEDINGS AND WILL BE RESTRICTED TO RESOLVING THE INDIVIDUAL DISPUTES BETWEEN THE PARTIES.

Id.

c. Events Leading Up To This Litigation.

On December 2, 1999, Mr. Ashby died. Pet. App. 8a. Mrs. Ashby filed a claim for the death benefit provided under the credit life insurance policy, but her claim was denied. Merit Life alleged that Mr. Ashby had answered questions about his health inaccurately. *Id.* Mrs. Ashby alleges that Anderson never asked them questions about Mr. Ashby's health. *Id.*

2. Procedural Background

On April 17, 2000, Mrs. Ashby filed this action in Limestone Circuit Court against AGF, Merit Life, and Anderson on her own behalf and in her capacity as representative of the estate of her deceased husband. Pet. App. 8a. Her complaint alleges fraud, fraudulent suppression, promissory fraud, conspiracy, breach of

contract, negligence, and bad-faith refusal to pay an insurance claim, and she seeks compensatory and punitive damages.

Defendants moved to stay the proceedings and to compel arbitration. Mrs. Ashby opposed the motion, asserting that the arbitration agreements were unconscionable and were obtained through fraud. *Id.* at 8a.

a. The State Trial Court Proceedings.

The trial court held two hearings on defendants' motion to stay the proceedings and to compel arbitration, during which it heard testimony from both Anderson and Mrs. Ashby. *Id.* at 59a. The trial court also considered briefs, affidavits, and documentary evidence submitted by the parties. *Id.* At the defendants' request, the trial court deferred ruling on the motion until after the United States Supreme Court addressed AGF's Petition for Certiorari in *AGF Inc. v. Branch*, 793 So. 2d 738 (Ala. 2000). The Court denied the petition on October 9, 2001, 534 U.S. 949 (2001), and the trial court issued its decision shortly thereafter.

The trial court found that Mr. Ashby was totally illiterate, and that Mrs. Ashby is "functionally illiterate" and "incapable of understanding the contract solely from an attempt to read it." *Id.* at 60a. Anderson knew the Ashbys could not read and comprehend the contracts. *Id.* Although he acknowledged that he had received no

training from AGF about how to explain arbitration agreements to consumers, he stated that he had explained those terms to the Ashbys. *Id.* at 7a. Mrs. Ashby disputed this assertion, testifying that Anderson had never explained the arbitration provisions in the loan and credit life insurance documents. *Id.* at 7a, 60a. After considering the conflicting testimony of Anderson and Mrs. Ashby, the court found that "Mr. Anderson did not inform Mr. and Mrs. Ashby that they were signing an arbitration agreement." *Id.* at 60a.

The trial court next concluded that the arbitration provision in the AGF loan document is unconscionable under Alabama Code 1975 § 5-19-16. First, the court concluded that the terms of the provision are "grossly favorable" to defendant because it is one-sided: the provision requires the borrower to arbitrate any and all disputes while leaving the lender free to seek relief in court, and it limits the amount an arbitrator can award to a borrower while "allow[ing] the lender to seek full redress for [its] claims in court." *Id.* at 62a-63a. In addition, the trial court concluded that Anderson's "refusal" "to explain, or even mention, the arbitration clause" is an "indicium of unconscionability." *Id.* at 64a. Second, the court found that AGF had "overwhelming bargaining power" because the Ashbys had no input in the drafting of the documents and no "meaningful choice" about whether to agree to those terms. *Id.* at 65a.

Finally, the trial court addressed the Ashbys' allegations that the arbitration provisions in the contracts

were procured by fraud. Because the court had found that the arbitration provision in AGF's loan agreement is unconscionable and thus unenforceable, it did not reach the question in relation to that contract. *Id.* at 66a. However, turning to the arbitration provision in the credit life insurance contract, the court found that there was "substantial evidence" of "fraud in the factum" — that is, fraud in the execution of the contract — because Mr. Ashby signed the contract without knowledge that it contained an arbitration provision. The court ordered the fraud claim to go forward to a jury, as required by Alabama law. *Id.* at 66a-67a.

b. The Alabama Supreme Court's Decision.

The Alabama Supreme Court affirmed the trial court's judgment, holding that AGF's arbitration clause is unconscionable.

The court agreed with the trial court that the question whether the arbitration clause is unconscionable must be addressed by a court before the parties can be ordered to arbitrate, and that the provision requiring arbitration of arbitrability disputes takes effect only after a court determines that the arbitration clause itself is enforceable. The court noted that this conclusion was in accord with its decision in *American General Finance, Inc. v. Branch*, 793 So. 2d 738 (Ala. 2000), *cert. denied* 534 U.S. 949 (2001), in which the court had held that when a party contests the validity "of the arbitration agreement itself, as opposed to the contract as a whole, the

court, and not the arbitrator, resolves the issue." *Id.* at 10a, 11a (citing *Branch*, 793 So. 2d at 748) (internal quotation marks omitted).

The Alabama Supreme Court also affirmed the trial court's conclusion that the arbitration agreement in AGF's contract with Mrs. Ashby is unconscionable, applying a two part test to determine unconscionability that looks to 1) whether the contract's terms are grossly favorable to a party that 2) has overwhelming bargaining power. *Id.* at 12a.

The court found that the terms of the arbitration agreement were grossly favorable to AGF because the clause requires arbitration of "every cause of action that could conceivably arise in favor of [Mrs. Ashby] and to every individual against whom a claim could conceivably be brought," including a claim concerning arbitrability, while at the same time giving AGF the freedom to choose a judicial forum for any cause of action it might have against Mrs. Ashby. *Id.* at 12a (quoting *Branch*, 793 So. 2d at 748), 16a-17a. In addition, the agreement limited Mrs. Ashby's legal remedies, but allowed AGF to obtain full redress of its claims in court. *Id.* at 16a. The court found a further indication of unconscionability in the fact that although the "Ashbys requested that the defendants explain the terms of the contract to them," Anderson "chose not to explain, or even mention, the arbitration clause." *Id.* at 14a.

The court next concluded that AGF had

overwhelming bargaining power because the Ashbys had no "meaningful choice" about whether to sign an agreement requiring arbitration. *Id.* at 16a. Mrs. Ashby was unaware that the agreement contained an arbitration provision because she is functionally illiterate and Anderson did not inform her of the existence of the arbitration agreement when she signed the contract. *Id.* at 21a. In addition, a survey of the market for consumer loans demonstrates that all of the companies providing such loans mandated arbitration. *Id.* at 19a. Finally, the Ashbys had no input in negotiating the terms or drafting the arbitration agreement. *Id.* at 21a.

The court also agreed with the trial court that the question whether the arbitration agreement in the Merit Life application for credit life insurance was obtained by fraud should be sent to a jury.

REASONS FOR DENYING THE WRIT

There is no reason for this Court to review the narrow and fact-specific holding of the Alabama Supreme Court in this case. The Alabama Supreme Court's conclusion that courts, and not arbitrators, must first decide the validity and enforceability of arbitration agreements before compelling arbitration is fully consistent with the express language of the Federal Arbitration Act (FAA) and with this Court's opinions. Moreover, although petitioners claim there is a conflict in the circuit courts, they have not identified a single case where a court ordered a party into arbitration under the

FAA for the threshold determination of whether the arbitration provision is unconscionable and therefore unenforceable.

In addition, the Alabama Supreme Court's holding that the arbitration agreement is unconscionable is fully consistent with Alabama law and with the FAA's saving clause that acknowledges that arbitration agreements should not be enforced to the extent that they conflict with state contract laws of general application.

I. The Decision of the Alabama Supreme Court is Consistent with this Court's Decisions.

The Alabama Supreme Court's holding that a court must decide whether an arbitration clause is unconscionable before compelling the parties to enter arbitration is a routine application of the express provisions of the FAA. Section 2 of the FAA states that contractual arbitration clauses are enforceable "save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. Likewise, section 4 empowers courts to compel arbitration of particular disputes only "upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue." 9 U.S.C. § 4. In keeping with these provisions, this Court has long held that "arbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed to so submit." *AT&T Technologies v. Communication Workers*, 475 U.S. 643, 648 (1986) (internal quotation marks

omitted).

Based on this principle and the above-quoted provisions of the FAA, this Court has drawn a sharp distinction between issues concerning the validity of an arbitration agreement, which a court must decide before it can order arbitration of a dispute, and other issues relating to contracts with arbitration provisions, which may be reserved for the arbitrator if the arbitration clause itself is enforceable. Notably, in *Prima Paint Corp. v. Flood & Conklin Mfg Co.*, 388 U.S. 395 (1967), the Court held that a claim of fraud in the inducement of a contract containing an arbitration clause is subject to arbitration, but that a claim of fraud in the inducement of an arbitration clause itself is for a court to decide under the FAA. *Id.* at 403-04. The Court explained:

> This position is consistent . . . with the [FAA's] statutory scheme. As the "saving clause" in § 2 indicates, the purpose of Congress in 1925 was to make arbitration agreements as enforceable as other contracts, but not more so. To immunize an arbitration agreement from judicial challenge on the ground of fraud in the inducement would be to elevate it over other forms of contract — a situation inconsistent with the "saving clause."

Id. at 404 n.12. Here, the Alabama Supreme Court's conclusion that a court, rather than an arbitrator, must

decide whether a contractual arbitration clause is valid and enforceable is fully consistent with the holding of *Prima Paint.*

Petitioners' attempt to establish a conflict between the decision below and *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938 (1995), fails because *First Options* did not undermine or cut back on the holding of *Prima Paint* by suggesting that if an arbitration agreement contains an "arbitration of arbitrability" clause, then disputes about whether the parties ever entered into a valid agreement to arbitrate must be reserved for the arbitrator. In *First Options*, this Court held that courts should decide whether a dispute was arbitrable *unless* the parties had clearly entered into a valid agreement stating that an arbitrator should decide those issues. That is, "the question 'who has the primary power to decide arbitrability' turns upon what the parties agreed about *that* matter." *Id.* at 944. Because the parties in *First Options* had never agreed to arbitrate arbitrability questions, they could not be compelled to arbitrate that question. Likewise, here, Mrs. Ashby contends that she never entered into a valid and binding agreement to arbitrate *any* issue — including questions regarding arbitrability — and thus, consistent with both *Prima Paint* and *First Options*, she cannot be compelled to arbitrate issues that she did not agree to submit to arbitration.

Thus, *First Options* did not reverse this Court's holding in *Prima Paint* that a party cannot be ordered into arbitration *before* there is a determination that the asserted

arbitration agreement is a valid and enforceable contract. Indeed, in discussing the problem of whether a court or an arbitrator should decide arbitrability, *First Options* made clear that the FAA's saving clause fully applies. The Court explained:

> When deciding whether the parties agreed to arbitrate a certain matter (including arbitrability) courts generally (though with a qualification we discuss below) should apply ordinary state-law principles that govern the formation of contracts.

Id. at 944.[1]

One of the "ordinary state-law principles that governs the formation of contracts" is whether the agreement is unconscionable under state law. *See, Doctor's Assocs., Inc. v. Casarotto*, 517 U.S. 681, 687 (1996) ("[G]enerally applicable contract defenses, such as fraud, duress or unconscionability, may be applied to invalidate arbitration agreements without contravening § 2."). Even when, as here, an arbitration provision requires the parties to arbitrate questions of arbitrability, the "saving clause" of the FAA still requires that courts pass upon the validity of the arbitration clause itself before mandating arbitration, as does § 4 of the FAA, which only

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[1] The "qualification" the Court referred to is that courts should not assume that the parties agreed to arbitrate arbitrability unless there is "clear and unmistakable" evidence that they did so. *Id.* at 944.

permits courts to compel arbitration "upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue." 9 U.S.C. § 4. Any other rule would "immunize an arbitration agreement from judicial challenge," and would "elevate it over other forms of contract — a situation inconsistent with the [FAA's] 'saving clause.'" *Prima Paint*, 388 U.S. at 404 n.12.

The decision below is thus consistent with *Prima Paint* and *First Options* in holding that a court must decide whether an arbitration clause is valid and enforceable before it may compel arbitration of any dispute.

II. The Alabama Supreme Court's Decision Does Not Conflict with Decisions of Other Courts.

Petitioners have cited no cases contravening the decision below by holding that an arbitrator decides the question whether an arbitration provision is unconscionable when the parties had agreed to arbitrate disputes about arbitrability. The cases that petitioners do cite are not at odds with the Alabama Supreme Court's opinion because they do not address the question whether a court, rather than an arbitrator, may decide whether the parties entered into a valid and enforceable agreement in the first instance.

For example, petitioners claim that *Apollo Computer, Inc. v. Berg*, 886 F.2d 469 (1st Cir. 1989), conflicts with the decision below. However, in *Apollo*,

neither party questioned the validity of the making of the arbitration agreement. Instead, plaintiff argued that the defendant could not compel arbitration because plaintiff had recently attempted to terminate that agreement. *Id.* at 472. The First Circuit's view that the question whether plaintiff had successfully terminated a once-binding arbitration agreement is reserved for an arbitrator is not at odds with the Alabama Supreme Court's decision that a court, not an arbitrator, must decide if a valid and enforceable arbitration agreement existed between the parties *in the first instance.*

Similarly, in all the other cases cited by petitioners, the parties did not dispute the existence of a valid, enforceable arbitration agreement, but rather disagreed about whether their disputes fell within the *scope* of that agreement. *See Shaw Group, Inc. v. Triplefine International Corp.*, 322 F.3d 115 (2d Cir. 2003) (parties disputed whether arbitration agreement required them to arbitrate claim for attorneys' fees and costs); *FSC Securities Corp. v. Freel*, 14 F.3d 1310 (8th Cir. 1994) (parties disputed whether arbitration was barred by six-year statute of limitations period in arbitration agreement); *United Food and Commercial Works Union v. Lucky Stores*, 806 F.2d 1385 (9th Cir. 1986) (Lucky claimed it was not required to arbitrate claim brought by union because union failed to specify "exact nature" of its claim, as arbitration agreement required); *Washington-Baltimore Newspapers Guild, Local 35 v. The Washington Post*, 959 F.2d 288 (D.C. Cir. 1992) (Post argued that issue Guild sought to arbitrate was not within scope of arbitration

agreement).

In all these cases, the courts decided that because the parties had explicitly agreed to arbitrate questions about arbitrability, it was for the arbitrator to decide if their disputes fell within the scope of the arbitration agreement. *See, e.g., Washington-Baltimore Newspaper Guild*, 959 F.2d at 29. As the D.C. Circuit explained, when the parties to an agreement give the arbitrator the power to decide arbitrability, the parties must "submit to arbitration all questions concerning the *meaning* of the arbitration clause." *Id.* (emphasis added). None of these courts suggested that the question whether the parties had, in fact, entered into a valid and enforceable arbitration agreement in the first instance was similarly reserved to the arbitrator. In short, these cases stand for the proposition that disputes over the "meaning of the arbitration clause" are to be decided by an arbitrator, *see id.*, but do not conflict with the Alabama Supreme Court's decision that disputes over the existence of a valid and enforceable arbitration clause are not.

Moreover, those courts that have addressed the specific issue in this case have reached the same conclusion as the Alabama Supreme Court below. For example, in *Luna v. Household Finance Corp. III*, 236 F. Supp. 2d 1166 (W.D. Wash. 2002), the court stated that the inclusion of a *First Options* clause within an arbitration agreement "does not limit a court's power to invalidate an arbitration agreement because, for reasons such as fraud, duress, or unconscionability the parties never validly

entered into the agreement." *Id.* at 1173. *See also Plattner v. Edge Solutions, Inc.*, No. 03-2646, 2003 WL 22859532 (N.D. Ill. Dec. 2, 2003); *Prevot v. Phillips Petroleum Co.*, 133 F. Supp.2d 937, 939-40 (S.D. Tex. 2001) (holding issue of unconscionability of arbitration clause is always a question for the court); *AGF v. Branch*, 793 So. 2d 738 (Ala. 2000), *cert. denied*, 534 U.S. 949 (2001)

In sum, the court below held that a party cannot be forced into arbitration under the FAA until a court has first determined that an asserted arbitration agreement, including one that provides for arbitration of arbitrability disputes, is a valid and enforceable contract under generally applicable state law. Petitioners have identified no decision holding the contrary and therefore have established no basis for this Court to grant review on the first question presented.

III. The Holding that Petitioner's Arbitration Clause is Unconscionable is Both Fact-Specific and Consistent with Prevailing Authority on State Contract Law and Federal Preemption.

The Alabama Supreme Court's decision is consistent with the FAA's command that arbitration provisions be subject to the same rules of state law that apply to other contracts. In *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681 (1996), the Court explained that Section 2 of the FAA places arbitration agreements on the same footing with other contracts so that "generally applicable contract defenses such as fraud, duress, or

unconscionability, may be applied to invalidate arbitration agreements without contravening § 2." *Id.* at 687. Likewise, in *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991), the Court noted Section 2's savings provision and warned that "'courts should remain attuned to well-supported claims that the agreement resulted from the sort of fraud or overwhelming economic power that would provide grounds for the revocation of any contract.'" *Id.* at 33 (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 627 (1985) (internal quotation omitted)). The court below did just this, applying previously recognized and generally applicable indicia of unconscionability under Alabama law and finding these indicia to have been established through a detailed evidentiary record.

The Alabama Supreme Court held that AGF's arbitration clause is unconscionable using the same indicia of unconscionability that the court has applied for more than ten years to cases that do not involve arbitration. *See Layne v. Gardner*, 612 So. 2d 404, 408 (Ala. 1992). The court based its finding that Mrs. Ashby had no meaningful choice as to arbitration and was subject to AGF's overwhelming bargaining power on an evidentiary record that demonstrated that nearly every lender required arbitration during the time period in question, and that AGF had made arbitration a mandatory condition for its loans. Petitioners mistakenly assert that, outside the context of arbitration agreements, Alabama courts had not held that market prevalence is relevant to an unconscionability analysis. Pet. 25. However, in *Lloyd v.*

Service Corp. of Ala., Inc., 453 So. 2d 735 (Ala. 1984), the Alabama Supreme Court relied on the prevalence of exculpatory clauses in landlord-tenant contracts in concluding that such a contract is unconscionable, finding that:

> The tenant has no meaningful choices. He can accept this landlord or go to another landlord who charges the same rent and asks the tenant to sign the same standard form lease. In other words, the modern standard form lease is in essence an adhesion contract. A survey of residential leases in Alabama would show that almost all contain these exculpatory clauses.
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> . . . [The] consumer, in need of goods or services, is frequently not in a position to shop around for better terms, because all competitors use the same clauses.

Id. at 739 (quoting *Taylor v. Leedy & Co.*, 412 So. 2d 763, 766 (Ala. 1982) (Faulkner, J., concurring)). In sum, the court's decision was based on longstanding, generally applicable principles of Alabama contract law.

Moreover, that Mrs. Ashby had no meaningful choice but to sign the agreement was not the only reason the court found the contract to be unconscionable. The Alabama Supreme Court nowhere said that market prevalence of a contractual term *by itself* renders the term

unconscionable. Instead, the court invoked widely recognized standards of substantive unconscionability in holding that the terms of AGF's particular arbitration clause are one-sided and unreasonably favorable to AGF.

The court emphasized that AGF's arbitration provision is unconscionable because it would require arbitration of all of Mrs. Ashby's claims (including those relating to arbitrability) and would limit her remedies should she prevail in arbitration, but would carve out from this requirement every foreseeable claim that petitioners might ever have. Pet. App. 16a-17a. Petitioners argue that the Alabama Supreme Court's reliance on the sweeping nature of the arbitration provisions as evidence of unconscionability is proof that the court was "hostile" to arbitration. Pet. 20-23. However, it was not the fact that the Ashbys were required to arbitrate all of their disputes that troubled the court, but rather the one-sided nature of a provision that limited the Ashbys to arbitration, and limited their remedies, while giving AGF the choice of *either* an arbitral or judicial forum in which to bring its claims and leaving AGF free to obtain all the relief available to it under law. A sizable body of case law from courts around the country has similarly treated such non-mutuality as an indicium of unconscionability.[2]

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[2] *See, e.g., Armendariz v. Foundation Health Psychare Services, Inc.*, 6 P.3d 669, 692-94 (Cal. 2000) (arbitration clause in employment contract is unconscionable where it applies only to employee's claims and places unilateral limits on employee's damages: "The unconscionable one-sidedness of the arbitration agreement is compounded in this case by the fact that it does not

Numerous courts have also recognized that arbitration provisions that limit a party's access to legal remedies that are available in court may also be unenforceable.[3]

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permit the full recovery of damages for employees, while placing no such restriction on the employer."); *Arnold v. United Companies Lending Corp.*, 511 S.E.2d 854, 861-62 (W. Va. 1998) (holding arbitration provision in lender's contract with elderly couple unconscionable because it contained a "wholesale waiver of the Arnold's rights together with the complete preservation of United Lending's rights.") (quotation omitted); *Showmethemoney Check Cashers, Inc. v. William*, 27 S.W.3d 361, 365-66 (Ark. 2000) (payday lender's arbitration clause is unenforceable under Arkansas contract law for lack of mutuality where lender's collection claims are exempted and all of the borrower's claims are covered); *Gibson v. Neighborhood Health Clinics, Inc.*, 121 F.3d 1126, 1131 (7th Cir. 1997) (arbitration clause in employment contract is unenforceable under Indiana law for want of consideration where clause applies to employee's claims but exempts employer's claims); *Hull v. Norton*, 750 F.2d 1547, 1550-51 (11th Cir. 1985) (arbitration provision in employment contract is unenforceable under New York law for want of consideration where employer reserves own right to sue in court; court finds no preemption because case falls within Section 2 saving clause).

[3] *See, e.g., Cole v. Burns Int'l Security Serv's*, 105 F.3d 1465, 1482 (D.C. Cir. 1997) (arbitration must offer "all the types of relief that would otherwise be available in court"); *Paladino v. Avnet Computer Technologies, Inc.*, 134 F.3d 1054, 1062 (11th Cir. 1998) (Cox, J., concurring for majority of court) (arbitrability of Title VII claims "rests on the assumption that the arbitration clause permits relief equivalent to court remedies.... When an arbitration clause has provisions that defeat the remedial purpose of the statute... the arbitration clause is not enforceable."); *Perez v. Globe Airport Security Services*, 253 F.3d 1280, 1286-87 (11th Cir. 2001) (holding arbitration clause that prevents prevailing Title VII plaintiff from

Petitioners argue that "mutuality of remedy is *not* a requirement for enforceability of a contract in Alabama. *See, e.g., Marcum v. Embry*, 282 So. 2d 49, 51 (Ala. 1973)." Pet. 24 (emphasis in original). Although petitioners are correct that mutuality of remedy is not a "requirement," it is certainly a relevant factor in determining whether a contract's terms are so unfair as to be unconscionable. Indeed, in *Marcum v. Embry* itself the court stated that a "[a] contract, lacking in mutuality, is unenforceable, because there is an absence of consideration moving[] from one party to the other." 282 So. 2d at 51. Although in *Marcum*, lack of mutuality in the contract at issue was not so severe as to demonstrate the complete absence of consideration, the court clearly considered lack of mutuality a relevant factor in

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recovering attorney's fees to be unenforceable); *DeGaetano v. Smith Barney, Inc.*, 983 F. Supp. 459, 469 (S.D.N.Y. 1997) (voiding arbitration clause disallowing attorney's fees for prevailing Title VII plaintiff, concluding that "contractual clauses purporting to mandate arbitration of statutory claims...are enforceable only to the extent that the arbitration preserves the substantive protections and remedies afforded by the statute."); *Lozada v. Dale Baker Oldsmobile, Inc.*, 91 F. Supp. 2d 1087, 1105 (W.D. Mich. 2000) (finding as to consumer Truth In Lending Act and state consumer protection act claims that "both federal and Michigan case law support a conclusion that an arbitration provision is substantively unconscionable because it waives class remedies, as well as declaratory and injunctive relief"); *Derrickson v. Circuit City Stores, Inc.*, 81 Fair Empl. Prac. Cas. 1533 (D. Md. 1999) (arbitration clause capping punitive damages and back pay remedies under Section 1981 is unenforceable), *aff'd*, 203 F.3d 821 (4th Cir.) (table), *cert. denied*, 530 U.S. 1276 (2000).

determining the fairness of a contract — just as the court did in its decision below. The holding of the court below is thus consistent with case law recognizing the need for courts to enforce general principles of state contract law in unusually one-sided and unfair circumstances to prevent businesses from abusing their bargaining power by turning private arbitration proceedings into occasions to diminish unilaterally the substantive legal rights of individual consumers.

Yet another significant factor in the court's unconscionability analysis was Anderson's failure to explain, or even mention, the arbitration provisions in AGF's contracts despite his knowledge that Mrs. Ashby is functionally illiterate. Although petitioners claim this issue was not relevant to the Alabama Supreme Court's unconscionability decision, *see* Pet. 14, they are mistaken. The Alabama Supreme Court found that the contract was unconscionable, in part, because even though the Ashbys "requested that the defendants explain the terms of the contract to them . . . defendant's agent chose not to explain, or even mention, the arbitration clause." Pet. App. 14a. In addition, the court reasoned that because Mrs. Ashby was unaware of the arbitration clause, she did not have the ability to negotiate the terms of that clause or shop for a lender who would not require her to arbitrate disputes, and thus she had "no meaningful choice" regarding arbitration. *See* Pet. App. 19a-20a.

Finally, petitioners contend that review is warranted here because Alabama courts are generally "hostile" to

arbitration. Pet. 29. Nothing supports this allegation. In the last few months alone the Alabama Supreme Court has compelled consumers into arbitration in numerous cases. *See, e.g., AmSouth Bank v. Looney*, 2003 WL 22977440 (Ala. Dec. 19, 2003); *Service Corp. Intern'l v. Fulmer*, 2003 WL 22872183 (Ala. Dec. 5, 2003); *Edward D. Jones & Co. LP v. Wehby*, 2003 WL 22753436 (Ala. Nov. 21, 2003); *Elizabeth Homes, L.L.C. v. Gantt*, 2003 WL 22520218 (Ala. Nov. 7, 2003). Indeed, a pending petition for writ of certiorari seeking review of a Ninth Circuit decision denying a motion to compel arbitration cites the Alabama courts as a *model* for appropriately applying state unconscionability rules to arbitration agreements. *See* Pet. for Cert., *Circuit City Stores v. Ingle*, No. 03-604 (filed Oct. 20, 2003), at 14-15. In short, the only arbitration provisions to which Alabama courts react with "hostility" are those that are unconscionable under Alabama law — which is just how the Alabama courts react to any type of unconscionable contract. Under the FAA, Alabama is free to refuse to enforce *any* contract that violates its generallyapplicable contract laws.

IV. The Question Presented Is Not Dispositive.

Another reason that this Court should not review the questions presented is that neither issue is dispositive of this case. Even if petitioners were correct that the Alabama trial court should not have passed on the unconscionability of the arbitration clause, the court would have found the arbitration agreement invalid and unenforceable on the ground that Mrs. Ashby did not

know that the agreement contained an arbitration provision.

After listening the testimony of the parties and considering affidavits, documents, and the parties' briefs, the trial court found that Mrs. Ashby is functionally illiterate and could not understand the contract simply by reading it. Pet. App. 60a. The court also found that Anderson knew that Mrs. Ashby was not capable of understanding the written contract, and yet he "did not inform Mr. and Mrs. Ashby that they were signing an arbitration agreement." *Id.* Thus, the Ashbys were unaware of the arbitration provision (including the clause requiring them to arbitrate all disputes about arbitrability). The Alabama Supreme Court noted, and relied upon, these factual determinations at several points in its opinions. Pet. App. 14a, 19a-20a.

Even petitioners acknowledge that "[u]nder *Prima Paint* and the Court's subsequent decisions, [] the dispositive question is whether the parties agreed that the issue of arbitrability would be submitted to the arbitrator." Pet. 13. As the trial court found, the Ashbys never agreed to arbitrate *any* dispute with petitioners. Pet. App. 60a. Thus, even if petitioners were correct that the Alabama courts should not have addressed the unconscionability question, the outcome in this case would be no different, because the Ashbys were not informed of the arbitration provisions in the contracts they signed and thus never agreed to arbitrate claims under those contracts.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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